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C O N F I D E N T I A L SECTION 01 OF 02 TBILISI 000057

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TAGS: [ECON](#) [ENRG](#) [PGOV](#) [PREL](#) [RU](#) [GG](#)  
SUBJECT: GEORGIA SIGNS MOU ON ENGURI WITH RUSSIAN FIRM RAO

REF: A. 08 TBILISI 1654  
[1](#)B. 08 TBILISI 1867  
[1](#)C. 08 TBILISI 2190  
[1](#)D. OLSON 1/12/09 E-MAIL

Classified By: Ambassador John F. Tefft for reasons 1.4 (b) and (d).

[1](#)1. (C) SUMMARY: First Deputy Minister of Energy Marika Valishvili confirmed that the Georgian Ministry of Energy and Russian electricity trader InterRAO signed on December 31 a ten-year Memorandum of Understanding (MOU) on joint management of the Enguri Hydropower Plant, located on both sides of the Abkhazia administrative boundary. The agreement will give 60 percent of the electricity output to Georgia and 40 percent to RAO, effectively replacing the long-standing agreement between the Georgians and Abkhaz. According to the agreement, Georgian engineers will continue to run the facility, overseen by a Georgian General Director. The Board of Directors will consist of an equal number of Georgians and Russians, but no Abkhaz. The Ministry of Energy hailed the agreement, as it now will be paid for electricity that had previously been provided for free to Abkhazia. In addition, the Ministry stressed it is now clear with whom they must deal on Enguri. RAO has also pledged to invest funds to strengthen the hydro-system by renovating inoperable power plants in Vardnili. Public opinion on this agreement has been decidedly negative, with many fearing that the government has now "sold" one of the country's most strategic assets to the Russians, at a time when the Russians are using similar assets to impact policy in Europe, and others concerned that the Government kept this agreement under wraps for nearly two weeks after the agreement was signed. However, from the Ministry's perspective, it is the best solution to a potentially crippling problem resulting from the August conflict and continued Russian pressure on Georgia. END SUMMARY.

BACKGROUND ) STRADDLING THE ADMINISTRATIVE BOUNDARY

[1](#)2. (C) Since the August conflict, the Enguri Power Station has been an area of possible conflict and concern. While the power station is located in Abkhazia, the dam is located on undisputed Georgian territory. The power station provides 40 percent of Georgia's winter electricity. Since the 1993-94 war in Abkhazia, the Georgians, in agreement with the Abkhaz, have run the power plant and provided Sukhumi electricity free of charge. Given Enguri's location and importance in the regional power grid, there has been much concern that the Abkhaz and/or Russians might move to annex the territory on which the dam is located. The pressure on the Ministry of Energy to keep Enguri power in the Georgia system has been acute, as has the pressure from the Russians and Abkhaz to either offer a sweetheart deal or risk confiscation and loss of control of the dam.

OPERATIONS TO CONTINUE AS NORMAL ) AGREEMENT DETAILS

[1](#)3. (C) Valishvili confirmed that the MOU had been signed between Georgian Minister of Energy Khetaguri and the Chairman of RAO UES Dod on December 31. According to Valishvili, the MOU envisions a Board of Directors that will

consist of an equal number of Georgians and Russians, but no Abkhaz. The Director General of the joint management company will be a Georgian, ensuring, in Valishvili's words, that all decisions will be beneficial for Georgia. The ten year joint management agreement gives Georgia control of 60 percent of the power produced and RAO-UES 40 percent. This breakdown mirrors the pre-existing ad hoc agreement between the Georgians and Abkhaz on power usage, except now the Georgians will be paid for the 520 MW of power that was formerly provided to the Abkhaz for free. RAO can use this power as it sees fit, which could include selling it to Sukhumi, or exporting it to Russia and Turkey. Daily operations will continue as normal, with Georgian engineers running the power plant and overseeing operations at the dam. Although the MOU was signed on December 31, 2008 the Minister of Energy only announced the deal publicly on January 12, after RAO leaked information to the press, creating public speculation that the Ministry was attempting to hide the deal.

#### LONG-TERM INFRASTRUCTURE INVESTMENT

14. (C) The MOU also provides for further development of the hydropower system by both parties. RAO has reportedly agreed to rehabilitate the existing, but inoperable, Vardnili 2, 3, and 4 power stations in Abkhazia. RAO has offered its shares in Telasi, its rights to Khrami 1 and 2 near Tbilisi, and its shares of thermal unit 9 at Gardabani as collateral to the Georgian Government. If RAO is unable to meet its investment obligations, then the Georgian Government will be able to take the above as "collateral."

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#### WHY DID THE GEORGIANS DO IT?

15. (C) Following the August conflict, there have been many questions about just which entity is in control of Enguri's power, and great uncertainty about the future (reftels). The pressure on the Georgian energy system, especially throughout the fall, was intense, as it was unclear if the Russians/Abkhaz would attempt to cut Enguri's power supply to Georgia by seizing the dam or turning off the power station on the Abkhaz side of the line. As discussions progressed on Enguri, it was extremely unclear to the Georgians with exactly whom they should negotiate. In an earlier meeting with the Ambassador, Minister Khetaguri said he had discussions with his counterpart in Abkhazia, then was going to fly to Turkey to meet with RAO in order to determine who called the shots. In ticking off the advantages to the agreement for Georgia, Valishvili stressed that the MOU provides long-sought clarity, since the Georgians will now have a precise partner and counterpart. (Embassy note. The fact that RAO controls electricity distribution in Tbilisi and did not cut the power during the August conflict with Russia may have added to Georgia's perception of RAO as a reliable commercial entity. End Note.) The agreement also provides the Georgians with much needed investment to further develop their hydropower system. In addition, Georgian will also now receive payment for the megawatts of power that was given away for free in the past. The Georgian Government also likely made the calculation that it will be much more difficult for the Russians or Abkhaz to completely cut Georgia off from Enguri, if doing so would also hurt their own bottom line.

#### COMMENT: WIN-WIN?

16. (C) While the Ministry of Energy appears to be optimistic about the deal, it has already been criticized in the press as "selling" one of Georgia's strategic assets to the Russians. The Ministry highlighted to post the positives of the agreement, namely clarity, money and infrastructure investment. It is clear the Ministry hopes this will bring some stability to the electricity situation, as the Russians

will be much less likely to grab the dam by military means if a Russian company is managing it. The agreement, as described, appears to give the Georgians the upper hand, especially as their own engineers will continue to run the plant. However, domestically, many are already questioning the reliability of a Russian partner in such a strategic asset and sector, given Russia's August invasion of Georgia. RAO's interest in this investment undoubtedly is based on the potential of the large Turkish market just beyond Georgia's doorstep, as well as the growing electricity market in Russia itself. In Turkey, RAO, as well as Georgia, can sell electricity at much higher rates to provide Turkey's peak summer demand. What is unclear, however, is how the Abkhaz will pay for the electricity that they have received for free for the last fifteen years, or indeed the Abkhaz view of this transaction. It will be interesting to see if RAO attempts to collect from Sukhumi, or if the Russians will pick up the expense. It is possible that if the Abkhaz are unable to pay, RAO might look to sell the electricity that had powered Abkhazia to other more profitable markets in Russia and Turkey, leaving Sukhumi literally in the dark.

TEFFT